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SUBJECT: ARMENIAN BRANDY: CHURCHILL'S FAVORITE FACES NEW THREATS

REF: A) TBILISI 871 B) TBILISI 419 C) YEREVAN 661

Sensitive But Unclassified. Please protect accordingly.

SUMMARY

¶11. (U) Standing on one end of Yerevan's "drunken" bridge, the Yerevan Brandy Company (YBC) is Armenia's leading exporter of brandy/cognac; a signature Armenian product, famous throughout the former-Soviet world. The company exports approximately 90 percent of its product, 75 percent to Russia. While recent changes in Russian excise stamp and phytosanitary regulations have hurt company sales, the larger threats facing the company are look-alike competitors and poor regulation of the industry. END SUMMARY.

AN IMPORTANT SOURCE OF INCOME FOR RURAL ARMENIA

¶12. (U) The YBC was founded in 1887 and was sold to French-beverage-giant Pernod Ricard in 1999 for USD 30 million. According to YBC President Herve Caroff, YBC holds the exclusive license for the Ararat Brandy trademark, a brandy so famous that is said to have been Winston Churchill's preferred drink. The company employs over 400 workers and has direct purchasing agreements with over 5,000 Armenian grape farmers who sell to collection facilities in three rural provinces. YBC also purchases grapes from Nagorno Karabakh. These facilities store and crush grapes and produce the distilled spirits which are blended and aged at the YBC factory in Yerevan.

SALES TO RUSSIA CRITICAL

¶13. (U) YBC sells approximately one third of its product during the New Year's-Russian Christmas holiday season. While the bulk of sales (75 percent) are to Russia, YBC is hoping to expand sales in Ukraine and other CIS countries. Total sales in 2005 were approximately 4.4 million liters, a rate which YBC hopes to match this year. YBC is also expanding its storage capacity, but because of the aging process, the impact of the expansion will not be felt for three to five years.

EXCISE STAMPS, FRAUD AND OTHER OBSTACLES

¶14. (SBU) One of the challenges faced by YBC this year has been the change in Russian excise stamp regulations in spring 2006. The

change occurred on very short notice and YBC had to airlift product with the new stamps to Russia to avoid running out of saleable supply in that market. Currently, YBC has the new stamps in stock and is producing to meet the anticipated holiday spike in demand, but according to Caroff, the company has a million-bottle stockpile in Russia with the old stamps which it cannot use.

¶ 15. (SBU) Russian phytosanitary regulations are also a concern to YBC. While YBC is confident that their product can meet the regulations, Caroff claims that other local Armenian producers are producing look-alikes to YBC's premium brands using imported wine spirits, substandard spirits or even grain spirits as a foundation. He is concerned that, as with Georgian wine (ref A), the Russians will decide to bar all brandy exported from Armenia as a result of this fraud. Caroff admitted, however, that the situation in Georgia was probably politically motivated and therefore such a crackdown against Armenian products was less likely.

¶ 16. (SBU) Caroff claims that official grape harvest statistics are exaggerated to conceal the illegal production of faux-brandy by YBC's competitors. In 2005, the grape harvest in Armenia was officially 130,000 tons, but Caroff claims that actual production was no more than 60,000. According to Caroff, companies which have been in existence for five or six years are selling "twenty-year old" brandy, a clear sign of fraud.

A LUCRATIVE BUSINESS FOR INFLUENTIAL PEOPLE

¶ 17. (SBU) Caroff also said that look-alike products are threatening YBC's market share. He complained about the Noy Wine and Brandy factory, which sits on the other side of the "drunken" bridge and is owned by influential businessman-turned-politician Gagik Tsarukyan

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(ref C). The Noy factory has the right to use the Ararat seal for its products, but was expected to use that seal for wines, not brandy. That firm recently has begun producing look-alike brandy of questionable provenance. Caroff told us he had spoken with the Ministry of Agriculture about setting up a commission to monitor brandy quality in Armenia, but was discouraged about the commission's prospects when he was told that brandy production had become a lucrative business for influential people.

GODFREY